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In the Supreme Court of the United States

OCTOBER TERM, 1952

No. 319

ROBERTS DAIRY COMPANY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The findings of fact and opinion of the Tax Court (R. 28-35) are unreported. The opinion of the Court of Appeals (R. 106-111) is reported at 195 F. 2d 948.

JURISDICTION

The judgment of the Court of Appeals was entered April 15, 1952. (R. 111-112.) A petition for rehearing (R. 113-119) was denied on May 7, 1952 (R. 121). By an order made by Mr. Justice Clark on July 22, 1952, the time for filing a petition for a

writ of certiorari was extended to and including September 8, 1952. The petition for a writ of certiorari was filed September 6, 1952. The jurisdiction of this Court is invoked under 28 U.S.C., Section 1254.

QUESTION PRESENTED

Whether the Court of Appeals correctly affirmed the decision of the Tax Court that the $750 payment made by the taxpayer to the National Tax Equality Association was not deductible from gross income as an ordinary and necessary business expense under Section 23(a)(1)(A) of the Internal Revenue Code.

STATUTE AND REGULATIONS INVOLVED

The pertinent provisions of the Internal Revenue Code and of Treasury Regulations 111 are set forth in the Appendix, *infra*.

STATEMENT

This is a proceeding involving excess profits taxes, brought to the Tax Court (R. 3-22) by petitioner, Roberts Dairy Company (hereinafter referred to as the "taxpayer"), in which, after the elimination of other issues, the only issue submitted to the Tax Court for decision was whether the sum of $750 paid by the taxpayer to the National Tax Equality Association (hereinafter referred to as "NTEA") in 1943 was deductible from its gross income, either under Section 23(a)(1)(A) or Section 23(q)(2) of the Internal Revenue Code (R. 29).

The facts, as found by the Tax Court [1] (R. 29-31) and as recited in the opinion of the court below (R. 107-111), may be summarized as follows:

The taxpayer, whose principal place of business is in Omaha, Nebraska, is engaged in the dairy business as an "independent," buying its milk from producers. In 1943 and prior years, the taxpayer was faced with severe competition from "cooperative" dairies, and had difficulty retaining its suppliers and customers because of the advantages the cooperatives, largely as a result of their tax-exempt status under Section 101(12) and (13) of the Code, were able to offer. (R. 29.)

To meet that competition, the taxpayer had the alternatives of changing itself into a "cooperative"; of showing to its customers and suppliers, by facts and statistics, the tax advantages of the cooperatives and thereby explaining its competitive position; or of ultimately achieving in some way a tax status equal to that of the cooperatives. To obtain aid from the services proposed by NTEA in meeting these problems, the taxpayer in October of 1943 paid $750 to NTEA, and subsequently received the bulletins, research publications and other literature distributed by NTEA. (R. 29-30.)

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[1] The facts were developed by a stipulation between the parties (R. 37-38), exhibits attached thereto (R. 39-67), some oral testimony (R. 74-97), and additional exhibits adduced in evidence at the hearing (R. 95, 96). The latter exhibits, designated as Petitioner's Exhibit 6 and Respondent's Exhibits A through G, by order of the court below (R. 100-101) were not included in the printed record, but copies or reproductions thereof in their original form were supplied to the court below and have been filed in this Court.

NTEA, a non-profit organization supported by contributions from its members, had been organized "to conduct educational, scientific and research activities relative to disparities in federal and state tax statutes" and "to disseminate such information * * * to the public and to federal and state governments." (R. 30.) NTEA was organized and primarily operated from its inception for the dissemination of propaganda designed to bring about a revision in the tax structure. (R. 31.) [2]

In his determination, the Commissioner disallowed the deduction for the $750 contribution to NTEA claimed by the taxpayer on its return for 1943. (R. 9, 10, 11.)

The Tax Court, upholding the Commissioner's action, held that the payment of $750 made by the taxpayer to NTEA in 1943 was not deductible from gross income, either as an ordinary and necessary business expense or as a contribution, under Section 23(a)(1)(A) or 23(q)(2), respectively. (R. 31-35.) The court below affirmed. (R. 107-111.)

ARGUMENT

1. Section 29.23(q)-1 of Treasury Regulations 111 provides that—

> Sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and

[2] Since this ultimate finding of fact by the Tax Court is not challenged before this Court (Pet. 5, 6), we omit from this statement a recital of any further evidentiary facts found by the Tax Court relative to NTEA (R. 30-31).

> contributions for campaign expenses are not deductible from gross income.

The identical provision of an earlier regulation, of long standing, has been upheld by this Court, and has been held applicable to deductions for expenditures claimed under Section 23(a) of the Code as ordinary and necessary business expenses. *Textile Mills Corp.* v. *Commissioner,* 314 U. S. 326.

The *Textile Mills* decision controls here. The Tax Court found (R. 31), and taxpayer accepts the finding (Pet. 6; cf. R. 70), that NTEA was organized and operated for the carrying on of propaganda seeking a revision of the tax laws. Accordingly, the Commissioner and the courts below were obviously correct in the view that taxpayer's payment to NTEA was not deductible as ordinary and necessary expenses under § 23(a), "since [it] clearly [runs] afoul of * * * the regulation." *Textile Mills, supra,* at 337.[3] There is no merit in the suggestion (Pet. 6-9, 12) that deductibility of the payment should be tested only "on the basis of the purposes and objectives of the taxpayer claiming the deduction," without regard to "the activities or purposes of the donee of the contribution" (Pet. 6). Both courts below have found (R. 34,

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[3] The taxpayer has abandoned here (cf. R. 32, 107) its argument that the contribution was deductible under Section 23(q)(2) of the Internal Revenue Code which expressly denies deductibility where a "substantial part of the activities of [the donee] is carrying on propaganda, or otherwise attempting, to influence legislation * * *."

110) that "the only reasonable purpose for the existence of NTEA [was] to influence legislation and contributions to it were used for that purpose." The attempt to evade the consequences of this finding by urging that the taxpayer's private purposes were different from those of the agency to which it gave its funds cannot alter or obscure the fact that the funds were "expended for * * * the promotion * * * of legislation * * * [and] the exploitation of propaganda * * * ."

The taxpayer not only fails to recognize that this case is governed by *Textile Mills,* but seeks (Pet. 9-10, 12-13) to show that the "decision of the Court of Appeals in affirming the Tax Court is a misconstruction of that decision and is necessarily in conflict with it" (Pet. 13). *Textile Mills,* the taxpayer argues, merely approved disallowance of a deduction where the sums are expended for "lobbying purposes" by a taxpayer in the "lobbying business." Even if this rigidly constricted reading of *Textile Mills* were warranted, there would be no basis for taxpayer's assertion of a "conflict." But it seems clear in addition that, in approving the validity of a regulation identical to the one in question and its applicability to the particular facts presented in *Textile Mills,* this Court made no such narrow distinction as the one taxpayer presses. Here, as there, the decisive fact is that the regulation, a clearly permissible interpretation of the statutory reference to "ordinary and necessary expenses", precludes the claimed deduction.

Even less substantial is the assertion (Pet. 6-7,

8, 9) that the courts below considered only Section 23(q)(2) and neither considered nor passed upon the argument that Section 23(a)(1)(A) authorized the deduction taxpayer sought. Both the Tax Court and the Court of Appeals unequivocally recognized (R. 29, 31-32, 107) that the taxpayer claimed the deduction alternatively, under either section. Both courts held that, on the facts of this case, Section 29.23(q)-1 of the Regulations (which applies to deductions claimed as business expenses under Section 23(a), *Textile Mills Corp.* v. *Commissioner, supra,* at 338) justified the disallowance of the deduction under either section.

2. The taxpayer argues (Pet. 13-17) that changes in the tax statutes and regulations since the *Textile Mills* decision require a different result here.[4] Since the taxable years involved in that case, the argument runs, Congress has specifically authorized deductions of charitable contributions by corporations, in what is now Section 23(q)(2) of the Code; the regulation involved in *Textile Mills* has been divided in two, and the presently relevant portion, Section 29.23(q)-1 of Regulations 111, applies only to deductions claimed for charitable contributions under Section 23(q)(2) of the Code; and, as a result of these changes, deductions for lobbying purposes claimed under Section 23(a)(1)(A) of the Code are "no longer specifically prohibited by regulation" (Pet. 17). But this is only a repetition of an argument made and briefly dis-

[4] This argument is made for the first time in this Court.

missed in the *Textile Mills* case where, applying the identical predecessor of the present regulation, this Court said the "argument that it was not applicable because it was not specifically incorporated under §23(a) is frivolous." 314 U.S. at 338. Phrased generally, the regulation says that sums like the one in dispute "are not deductible from gross income." The failure to repeat this restriction in regulations attached to every section under which such a deduction might be claimed is of no more weight here than it was in *Textile Mills.*

3. Finally, there is no merit in the contention (Pet. 17-20) that, in order to be non-deductible under Section 23(a)(1)(A), an expenditure must have been for something sinister, illegal, or profoundly repugnant to public policy. In support of this argument, taxpayer invokes the recent decision in *Lilly* v. *Commissioner,* 343 U.S. 90 (Pet. 19-20). There, however, as taxpayer acknowledges (Pet. 13), this Court emphasized that the decision in the *Textile Mills* case was distinguishable, turning on an interpretative regulation which "had itself been in effect many years with congressional acquiescence." 343 U.S. at 95. As we have shown, the instant case, unlike *Lilly,* comes "within that precedent." *Ibid.* The same regulation, enjoying still the acquiescence of Congress, has led to a similar result. The plain terms of the regulation have never been limited to preventing only deductions for illegal or shady purposes, and nothing in the *Lilly* case or any other indicates any reason why they should be so limited now. See *Bellingrath* v.

Commissioner, 46 B.T.A. 89; cf. *Sunset Scavenger Co.* v. *Commissioner,* 31 B.T.A. 758, 763, reversed, 84 F. 2d 453 (C.A. 9).

CONCLUSION

The decision below is correct. It turns upon the particular facts of the case and presents no question calling for further review by this Court. There is no conflict of decisions. The petition should, therefore, be denied.

Respectfully submitted,

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OCTOBER, 1952.

APPENDIX

Internal Revenue Code:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

(a) [as amended by Section 121 (a) of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Expenses.*—

(1) *Trade or Business Expenses.*—

(A) *In General.*—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; traveling expenses (including the entire amount expended for meals and lodging) while away from home in the pursuit of a trade or business; and rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity.

(B) *Corporate Charitable Contributions.*—No deduction shall be allowable under subparagraph (A) to a corporation for any contribution or gift which would be allowable as a deduction under subsection (q) were it not for the 5 per centum limitation therein contained and for the requirement therein

that payment must be made within the taxable year.

* * * * *

(q) [as amended by Section 1225 of the Revenue Act of 1942, *supra*] *Charittable and Other Contributions by Corporationss.*—In the case of a corporation, contributions or gifts payment of which is made within thee taxable year to or for the use of:

* * * * *

(2) A corporation, trust, or community chest, fund, or foundation, created or organized in the United States or in any possession thereof or under the law of the United States, or of any State or Territory, or off the District of Columbia, or of any possession of the United States, organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes or for the prevention of cruelty to children (but in the case of contributions or gifts to a trust, chest, fund, or foundation, payment of which is made within a taxable year beginning after the date of the cessation of hostilities in the present war, as proclaimed by the President, only if such contributions or gifts are to be used within the United States or any of its possessions exclusively for such purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual, and no substantial part of the activities of which is carrying on propa-

ganda, or otherwise attempting, to influence legislation;

to an amount which does not exceed 5 per centum of the taxpayer's net income as computed without the benefits of this subsection. Such contributions or gifts shall be allowance as deductions only if verified under rules and regulations prescribed by the Commissioner, with the approval of the Secretary.

* * * * *

(26 U.S.C. 1946 ed., Sec. 23.)

Treasury Regulations 111, promulgated under the Internal Revenue Code:

Sec. 29.23(a)-13. *Corporate Contributions.* No deduction is allowable under section 23 (a) for a contribution or gift by a corporation if any part thereof is deductible under section 23(q). Thus, for example, if a corporation makes a contribution of $5,000, only $4,000 of which is deductible under section 23(q) (whether because of the 5 percent limitation or requirement of actual payment, or both), no deduction is allowable under section 23(a) for the remaining $1,000.

The limitations provided in section 23(a)(1) and this section apply only to payments which are in fact contributions or gifts to organizations described in section 23(q). For example, payments by a street railway corporation to a local hospital (which is a charitable organization within the meaning of section 23(q) in consideration of a binding obliga-

tion on the part of the hospital to provide hospital services and facilities for the corporation's employees are not contributions or gifts within the meaning of section 23(q) and may be deductible under section 23(a) if the requirements of that section are otherwise satisfied. Donations to organizations other than those described in section 23(q) which bear a direct relationship to the corporation's business and are made with a reasonable expectation of a financial return commensurate with the amount of the donation may constitute allowable deductions are business expenses. For example, a street railway corporation may donate a sum of money to an organization (of a class not referred to in section 23(q)) intending to hold a convention in the city in which it operates, with a reasonable expectation that the holding of such convention will augment its income through a greater number of people using its cars.

* * * * *

Sec. 29.23(q)-1. *Contributions or Gifts by Corporations.*—A corporation may deduct from its gross income contributions or gifts to organizations described in section 23(q) (see section 29.22(b)(4)-1 for definition of "political subdivision") * * * Such deduction shall, to the extent provided by that section, be allowed only for the taxable year in which such contributions or gifts are actually paid, regardless of when pledged and regardless of the method of accounting employed by the corpo-

ration in keeping its books and records. As to charitable contributions by corporations not deductible under section 23(a), see section 29.23 (a)-13. Sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and contributions for campaign expenses are not deductible from gross income.

* * * * *

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